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Date March 8, 1994

Surname [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

JAN 24 1994

Employer Identification Number: [REDACTED]  
Key District: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code. For the reasons stated below, we have concluded that you do not qualify for tax exemption under this section. Your protest rights are also stated below.

You were incorporated on [REDACTED], under the nonprofit statute of [REDACTED]. Article [REDACTED] of your incorporating instrument states that you are organized exclusively for charitable and educational purposes, including the making of distributions to organizations that are tax exempt under Code section 501(c)(3). More specifically, you are organized to create, promote, and conduct science fiction conventions, which are described as "educational events which allow the public to meet, interact with, and learn from artists, writers, and educators in science and science fiction." Any profits derived from the conventions shall be used for future operating capital and for charitable distributions to qualified exempt organizations.

Article [REDACTED] contains language which prohibits the inurement of your net earnings to the benefit of any members, officers, or other private persons. It also provides that you shall not engage in any activities or exercise any powers that are not in furtherance of the purposes stated in Article [REDACTED]. Article [REDACTED] provides for a satisfactory distribution of any remaining assets upon your dissolution.

The introductory paragraph to your Bylaws states that, "... The principal fund-raising endeavor of the corporation is the

[REDACTED]

enactment of [REDACTED] Conventions on an annual or more frequent time frame."

Your first convention was held [REDACTED], at a resort hotel in [REDACTED]. It was called [REDACTED] (acronym for [REDACTED]). Approximately [REDACTED] people attended [REDACTED].

In response to Part II, 1 of Form 1023, exemption application, you describe a science fiction convention as an educational event which includes educators, authors, artists, stage magicians, and musicians. Scheduled workshops include professional writers and artists teaching their crafts and programming for children. In conformity with your incorporating instrument, you reiterate that all funds raised beyond those necessary to pay for the convention and to begin the planning of the next one will go to authorized charities, i.e., section 501(c)(3) qualified organizations.

In a letter dated [REDACTED], responsive to a development letter from the District Office dated [REDACTED], you elaborate upon the educational aspects by citing the topics discussed at [REDACTED], as follows: [REDACTED]

[REDACTED]. The foregoing topics were presented by writers of science fiction. In addition, the following panels were conducted by artists: [REDACTED]

[REDACTED] The convention also featured readings by [REDACTED] guest authors and a variety of workshops.

Aside from the educational activities above, the Programming Schedule for [REDACTED] indicates that this convention also features many activities of a social and recreational nature. This includes the operation of a gaming room, open 24 hours a day, a costume contest, a "slave auction", a massage workshop and belly dancing by one [REDACTED], and a Saturday night dance.

Your submission dated [REDACTED], includes a [REDACTED] Ledger" which is a record of income and expenses from [REDACTED], through [REDACTED]. Your income was derived from membership fees (\$[REDACTED] per member), table fees (ranging from \$[REDACTED] to \$[REDACTED]), donations (ranging from \$[REDACTED] to \$[REDACTED]), and "miscellaneous", which includes the [REDACTED]% commission paid by art dealers from their sales, consignment fees, and other items, including advertising and T-Shirt sales. You collected

██████████ in commissions from the art work sold by ████████ dealers, with ████████ dealers accounting for \$██████ (commissions paid of \$██████, \$██████, and \$██████). Consignment fees amounted to \$██████ from ████████ consignments, including fees of \$██████ and \$██████. Total revenue from ████████ amounted to \$██████ and total expenses were \$██████, leaving a net surplus of \$██████.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated "exclusively" for religious, charitable, educational, or other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order to qualify for exemption under Code section 501(c)(3), an organization must be both organized and operated exclusively for one or more exempt purposes. Failure to meet either the organizational or operational test will disqualify an organization from exemption under section 501(c)(3).

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish such purposes. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. Thus, in construing the meaning of the phrase "exclusively for educational purposes" in Better Business Bureau v. United States, 236 U.S. 279 (1945), 1945 C.B. 375, the Supreme Court of the United States stated, "This plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes."

Section 1.501(c)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for an exempt purpose unless it serves a public rather than a private interest. Thus, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

The case of St. Louis Science Fiction Limited v. Commissioner, T.C. memo. 1985-162, deals with a nonprofit organization whose principal activity is conducting an annual science fiction convention, called Archon, in St. Louis. The convention is widely advertised and open to the public. This was

the organization's sole activity for the first three years of its existence, until June, 1982, when it participated in the Space Week programs at a local planetarium. Also, the organization furnished a display on science fiction literature to the St. Louis Public Library during the summer of 1982.

Archon generally lasts from Friday evening to Sunday afternoon. At each convention, science fiction authors and personalities are present at readings and panel discussions. At the 1980 convention, other activities included a masquerade party, a pool party, a sing-along program, a 24-hour gaming room, movies, an art show and auction, and a huckster's room. Panel discussion topics included science fiction and fantasy films; advice on how to start a science fiction magazine; the psychology of horror; future worlds; and lobbying for the space program.

The organization derived its income from convention admission fees, table rental charges, art sales commissions, program advertising charges, and a small amount of contributions.

In its analysis, the Tax Court noted that the term "educational" is defined in section 1.501(c)(3)-1(d)(3)(i) of the regulations to include the following: "(a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or (b) the instruction of the public on subjects useful to the individual and beneficial to the community".

The court then commented as follows:

We have no doubt that some of petitioner's more serious panel discussions, e.g., "The Personal Apocalypse: The Relationship of Science Fiction/Fantasy to Role Playing Games", served an educational purpose. However, based upon our examination of the entire administrative record, we conclude that social and recreational purposes constituted a substantial portion of petitioner's activities. In the 1981 convention program, petitioner addressed its attendees as follows: "This year at Archon there is something for everyone: expanded gaming facilities with numerous tournaments, a huge movie room, a masquerade, a 24-hour hospitality room, your favorite pros, the largest art show ever put together at Archon and much, much more."

The Court concluded that,

Accordingly, although petitioner's conventions may have provided some educational benefit to the individuals involved, the predominance of social and recreational purposes compels us to conclude that petitioner has failed to establish that it is operated exclusively for educational purposes. See North American Sequential Sweepstakes v. Commissioner (Dec. 38,404), 77 T. C. 1087 (1981); Minnesota Kingsmen Chess Association, Inc. v. Commissioner {Dec. 40,370(M)}, T. C. Memo. 1983-495.

Moreover, we also agree with respondent that there is additional support for denying petitioner tax-exempt status. Petitioner's huckster's room and art auction provide substantial benefit to private interests. See Sec. 1.501(c)(3)-1(d)(1)(ii), Income Tax Regs. Revenues to private artists at the 1980 convention amounted to \$2,376.41. In 1981 the artists earned \$2,818.35 and in 1982, they earned \$4,800. We have no figures as to the amounts earned by individuals in the huckster's room but we know that about 50 tables were rented in 1980, and 75 in 1981. This Court has held previously that tax-exempt status is to be denied to organizations that substantially benefit private rather than public interests. Sec. 1.501(c)(3)-1(d)(1)(ii), Income Tax Regs.; Ecclesiastical Order of the ISM of Am, Inc. v. Commissioner {Dec. 40,078}, 80 T. C. 833 (1983), affd. without published opinion 740 F. 2d 967 (6th Cir. 1984); Christian Stewardship Assistance, Inc. v. Commissioner {Dec. 35,422} 70 T. C. 1037 (1978).

Petitioner relies heavily upon Goldsboro Art League, Inc. v. Commissioner {Dec. 37,441}, 75 T. C. 337 (1980), in support of its contention that it is tax-exempt. In Goldsboro Art League, the taxpayer was an organization that operated two art galleries that exhibited and sold artworks. We held that the taxpayer was tax-exempt under section 501(c)(3) because it was organized and operated exclusively for an exempt purpose-art education. We noted that in order to insure artistic quality and integrity, the artworks displayed were selected by jury procedures. We also noted that the taxpayer was the only such museum or gallery within its county, or any contiguous county. We held that it served public, rather than private interests and that its sales activities were incidental

[REDACTED]

to advancing its exempt purpose. By contrast, petitioner in this case did not apply any controls to insure the quality of the books and artworks sold at its convention. Also, the tone of petitioner's convention is substantially, if not predominantly social and recreational, rather than educational. In addition, petitioners' huckster's room and art auction provided substantial benefit to private interests that is not incidental to its exempt purpose. Consequently, we think the case Goldsboro Art League is clearly distinguishable on its facts from the instant case.

Inasmuch as the organizations failed to satisfy the operational test under section 1.501(c)(3)-1(c) of the regulations, the Court held that the organization does not qualify for tax exemption under section 501(c)(3) of the Code.

With respect to your own application, we believe that the decision in the above cited case is fully applicable to the facts presented. Thus, as indicated in our factual outline, the one annual convention which you have conducted to date, [REDACTED], was replace with social and recreational activities (aside from the activities of a clearly educational nature). Under section 1.501(c)(3)-1(c)(1) of the regulations, an organization will not meet the operational test under Code Section 501(c)(3) if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. See also the holding in the Better Business Bureau case, cited above.

You also do not satisfy the operational test under section 501(c)(3) because the sales of art work and consignment sales at your convention benefit private interests to a substantial degree. The amounts of commission paid by private art dealers indicate that three (3) of these individuals made sales in excess of \$[REDACTED]. This is in contravention of the requirements under section 1.501(c)(3)-1d(1)(ii) of the regulations. See also the holding in St. Louis Science Fiction Limited, above.

We conclude that you do not meet the operational test under Code section 501(c)(3) on the basis of the two grounds discussed above. Under section 1.501(c)(3)-1a(1) of the regulations, failure to meet either the organizational or operational test will disqualify an organization from exemption under Code Section 501(c)(3).

Based on the foregoing, we hold that you are not exempt from federal income tax under section 501(c)(3) of the Code. Therefore, contributions to you are not deductible under section

170 of the Code. You are required to file federal income tax returns on Form 1120.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practice Procedures.

If you do not protest this proposed ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the U.S. Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key District Director, Baltimore, Maryland, which is your key district for exempt organization matters. Thereafter, if you have any questions about your federal income tax status, including questions concerning reporting requirements, please contact your key District Director. The appropriate State Officials will be notified of this action in accordance with section 6104(c) of the Code.

[REDACTED]

When sending a protest or other correspondence with respect to this case, you will expedite its receipt by using the following address on the envelope:

Internal Revenue Service  
1111 Constitution Avenue, NW,  
Washington, DC 20224  
[REDACTED]

Sincerely,

[REDACTED]

Chief, Exempt Organizations  
Rulings Branch 4

cc: [REDACTED]

cc: [REDACTED]